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BEFORE THE ARIZONA CORPORATION COMMISSION

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Arizona Corporation Commission

DOCKETED

APR 12 2004

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In the matter of:

YUCATAN RESORTS, INC., d/b/a
YUCATAN RESORTS, S.A., RESORT
HOLDINGS INTERNATIONAL, INC., d/b/a/
RESORT HOLDINGS INTERNATIONAL,
S.A., WORLD PHANTASY TOURS, INC.,
a/k/a MAJESTY TRAVEL a/k/a VIAJES
MAJESTY, and MICHAEL E. KELLY,

Respondents.

DOCKET NO. S-03539A-03-0000

**WORLD PHANTASY'S
REPLY IN SUPPORT OF ITS
RENEWED MOTION TO
DISMISS AND MOTION FOR
SANCTIONS
—AND—
RESPONSE TO THE
DIVISION'S REQUEST FOR
SANCTIONS**

The Securities Division's Response ("Response") to World Phantasy's renewed motion to dismiss and motion for sanctions substitutes invective for substance.

Ignoring the uncharitable adjectives, the Division's position on the legal merits of World Phantasy's motion is:

Whether [World Phantasy] was providing and entering into contracts with investors as the investors' "independent" leasing agent, providing investors with their quarterly returns on their investments in the alleged form of "leasing profits," or (purportedly) acting as the servicing agent for the investors' Universal Lease timeshare units, [World] Phantasy was a key component to both the promotion and operation of the entire Universal Lease program.

1 Response, at 6-7. The same may be said of the U.S. Mail, telephone service, and the
2 printing companies with whom Yucatan Resorts contracted for brochures. Critically
3 missing from the Division's pleadings are any allegations that World Phantasy
4 committed any offense, much less one within the Division's jurisdiction. Also
5 tellingly missing from the Division's Response is any discussion of the actual
6 language contained in the Division's Amended Order. The dispute is, we submit, a
7 straightforward issue of law concerning the sufficiency of the Division's pleadings,
8 and is, therefore, readily decided without an evidentiary hearing. See Parks v. Macro-
9 Dynamics, Inc., 121 Ariz. 517, 519, 591 P.2d 1005, 1007 (App. 1979) (reciting that
10 motion to dismiss for failure to state a claim attacks legal sufficiency of the complaint,
11 and court assumes complaint's allegations are true).

12 The Division disagrees. It says that an administrative law judge is powerless to
13 protect World Phantasy from the expense of participating in extensive discovery and a
14 lengthy hearing despite the Division's failure to allege any culpable participation by
15 World Phantasy in any securities offense.

16 **1. The Sufficiency of the Division's Pleadings Is Readily Decided as a Matter**
17 **of Law**

18 World Phantasy bases its legal argument for dismissal on specific prior
19 decisions of the Corporation Commission. See Matter of Offering of Securities by:
20 American Microtel, Inc., Arizona Corp. Comm'n Decision No. 58088 (Dec. 9, 1992)
21 (declining to hold liable as participants or aiders and abettors respondents having no
22 involvement in solicitation activities and no decisional authority or oversight
23 responsibilities regarding the content or use of promotional literature). The Division
24 has not alleged that World Phantasy had (1) any involvement in solicitation activities,
25 or (2) any decisional authority or oversight responsibilities regarding the content or use
26 of any promotional literature. The Division has also failed to allege that World

1 Phantasy engaged in conduct both “necessary to,” and a “substantial factor in,” the
2 unlawful transaction. Microtel at 12 (citing S.E.C. v. Rogers, 790 F.2d 1450, 1456 (9th
3 Cir. 1986)).¹ And even that standard has been criticized as overly broad by the United
4 States Supreme Court:

5 The deficiency of the substantial-factor test is that it divorces the
6 analysis of seller status from any reference to the applicable
7 statutory language and from any examination of § 12 in the
8 context of the total statutory scheme. Those courts that have
9 adopted the approach have not attempted to ground their analysis
10 in the statutory language. Instead, they substitute the concept of
11 substantial participation in the sales transaction, or proximate
12 causation of the plaintiff's purchase, for the words “offers or sells”
13 in § 12. The “purchase from” requirement of § 12 focuses on the
14 defendant's relationship with the plaintiff-purchaser. The
15 substantial-factor test, on the other hand, focuses on the
16 defendant's degree of involvement in the securities transaction
and its surrounding circumstances. Thus, although the substantial-
factor test undoubtedly embraces persons who pass title and who
solicit the purchase of unregistered securities as statutory sellers,
the test also would extend § 12(1) liability to participants only
remotely related to the relevant aspects of the sales transaction.
*Indeed, it might expose securities professionals, such as
accountants and lawyers, whose involvement is only the
performance of their professional services, to § 12(1) strict
liability for rescission. The buyer does not, in any meaningful
sense, “purchas[e] the security from” such a person.*

17 Pinter v. Dahl, 108 S.Ct. 2063 (1988) (internal footnotes omitted; emphasis added);
18 see also State v. Gunnison, 127 Ariz. 110, 112-13, 618 P.2d 604, 606-07 (1980)
19 (“Unless there is a good reason for deviating from the United States Supreme Court's
20 interpretation, we will follow the reasoning of that court in interpreting sections of our
21 statutes which are identical or similar to federal securities statutes.”).

22 The Division makes exactly the claim the Supreme Court sought to guard
23 against in Pinter v. Dahl. Because an “investor” is free to use any leasing agent it
24 wants, so-called “investment returns” do not depend on contracting with World

25
26 ¹ For a description of conduct that the 9th Circuit found insufficient to impose participant
liability, see Rogers at 1457. The Division has not made allegations against World
Phantasy even approaching the insufficient level of involvement described in Rogers.

1 Phantasy as the particular leasing agent. Hence, the Division seeks to impose liability
2 upon a mere property manager whose sole involvement is the performance of
3 professional services.

4 In place of specific allegations, the Division crafts the appearance of
5 participatory conduct, without actually alleging anything. For example, by using of
6 the term "whether" to begin its introductory phrase, the Division does not actually
7 allege that World Phantasy provided contracts or investment returns. And instead of
8 alleging that World Phantasy "disburses purported investments proceeds to investors,"
9 the Division does nothing more than argue that the hypothetical maid service does not.

10 Even setting aside the issue of whether or not the Division even makes these
11 claims, the fact remains that no such allegations were made in the Division's
12 pleadings. In now two responses to World Phantasy's motion to dismiss for failure to
13 plead essential elements of securities laws violations, the Division has yet to identify a
14 single paragraph of either the original Order or the Amended Order that states a claim
15 against World Phantasy. If, for example, the Division is prepared to allege that World
16 Phantasy *actually provided* Universal Lease Agreements to "investors," then the
17 Division should seek leave to amend the Amended Order to reflect that allegation.
18 Making a vague accusation to this effect in response to a motion to dismiss does not
19 change the language used in the Division's pleadings.

20 Indeed, the Division's response flies in the face of the law of the case as
21 established by this Court's prior rulings. If the Division is correct that (1) this Court
22 lacks jurisdiction to dismiss claims which are invalid on their face, or (2) that
23 allegations of non-culpable association with other respondents are sufficient to "state a
24 claim," the Division necessarily contends that this Court had no power to dismiss Mrs.
25 Kelly.

1 **2. An Expeditious Decision On the Merits of World Phantasy's Motion Is**
2 **Proper and Warranted**

3 As it now must, the Division admits that not a single one of the orders “in my
4 brief case” directs World Phantasy to do anything—or even substantively mentions it
5 at all. But the Division is unrepentant. In its view, apparently, being the Division
6 means never having to say, “I’m sorry.”

7 With its characteristic disregard for Due Process, the Division argues that the
8 administrative rules effectively prevent a respondent from obtaining a ruling on a
9 motion to dismiss—regardless of the circumstances—until an evidentiary hearing is
10 held. In other words, according to the Division, a respondent is not entitled to know
11 what it supposedly did that violates Arizona’s securities laws: it must apparently wait
12 for the evidentiary hearing in order to find out. The law, on the other hand, imposes
13 no such burden. See Weatherford v. State, 206 Ariz. 529, ¶ 11, 81 P.3d 320, 324
14 (2003) (“The Due Process Clause is intended to prevent government officials from
15 abusing their power or employing it as an instrument of oppression.”). It is a
16 fundamental tenet of Due Process—applicable to administrative proceedings as well as
17 trials—that the charging papers must describe an offense against the respondent. See
18 e.g., Bowman Transp., Inc. v. Arkansas-Best Freight Sys., Inc., 419 U.S. 281, 288, 95
19 S. Ct. 1502, 1514 (1974) (“A party is entitled, of course, to know the issues on which a
20 decision will turn and to be apprised of the factual material on which the agency relies
21 for decision so that it may rebut it.”); Chicago, Milwaukee, St. Paul & P. R. Co. v.
22 United States, 585 F.2d 254, 260 (7th Cir. 1978) (“Fundamental fairness in
23 administrative proceedings requires notice clearly informing a party of the proposed
24 action and the basis for that action.”); Standard Oil Co. v. Federal Trade Comm’n, 475
25 F.Supp. 1261, 1273 (N.D. Ind. 1979) (“It is beyond dispute that the traditional
26 concepts of procedural due process apply with full force to administrative proceedings,

1 and that administrative agencies are bound by the requirements of procedural due
2 process to give a defendant prompt notice of the factual predicates of the government's
3 case.").

4 In this context, ironically, the Division embraces as law of the case this Court's
5 initial decision to take motions to dismiss for lack of subject matter jurisdiction under
6 advisement pending an evidentiary hearing before the Commission. But World
7 Fantasy respectfully submits that the reasoning employed does not apply to its
8 motion, and furthermore, that the situation has changed sufficiently to warrant
9 revisiting the issue. World Fantasy draws the Court's attention to the fact that the
10 decision to take motions to dismiss under advisement, and the basis for doing so, was
11 discussed during the July 17, 2003 Pre-Hearing Conference—a conference at which
12 World Fantasy was not represented because it had yet to appear in the proceedings—
13 and referenced primarily motions to dismiss on the issue of whether the contracts at
14 issue constituted securities.² [Jul. 17, 2003 Pre-Hearing Conference, 8/4-13/16]
15 World Fantasy cannot be bound by rulings resolving a controversy in which it did not
16 participate. See Hall v. Lalli, 194 Ariz. 54, 57, 977 P.2d 776, 779 (1999) ("It is a rule
17 as old as the law that no one shall be personally bound until he has had his day in
18 court."); Webb v. Arizona Board of Medical Examiners, 202 Ariz. 555, 558, ¶ 9, 48
19 P.3d 505, 508 (App. 2002) ("Procedural due process requires notice and opportunity to
20 be heard in a meaningful manner at a meaningful time.").

21 In any event, the discussion at the July 17, 2003 Pre-Hearing Conference
22 indicated substantially more flexibility with respect to motions to dismiss for lack of
23

24 ² World Fantasy did not appear until August 8, 2003 when it filed its answer, request for
25 hearing, and motion to dismiss. The Third Procedural Order memorializing the Court's
26 decision to take the motions to dismiss under advisement pending an evidentiary hearing
was issued on September 12, 2003. The first Pre-Hearing Conference after World
Fantasy's appearance occurred on October 7, 2003.

1 personal jurisdiction, for example. [Jul. 17, 2003 Pre-Hearing Conference, 17/12-
2 21/1] And contrary to the Division's assertions, one respondent was, in fact, dismissed
3 without prejudice by procedural order on November 21, 2003 for failure to effect
4 personal service. Where the issue is solely whether, based on a plain reading of the
5 Amended Order, the Division has stated a claim for violation of Arizona's securities
6 laws, no evidence is required to properly dispose of a motion to dismiss. See Stehney
7 v. Perry, 907 F.Supp. 806, 821-22 (D. N.J. 1995) (holding that "[w]here the facts are
8 not in dispute, due process no more requires an evidentiary hearing in the
9 administrative context than it does in the judicial context. Accordingly, this Court
10 finds that Count II of plaintiff's complaint has no merit, and defendants' motion to
11 dismiss this claim pursuant to Fed.R.Civ.P. 12(b)(6) is granted.").

12 **3. Conclusion**

13 World Phantasy therefore reiterates its position that it is fundamentally unfair to
14 put World Phantasy to the expense of continuing to defend a complex and long-
15 pending case based upon the non-cognizable allegations contained in the Division's
16 Amended Order. See State v. Casey, 205 Ariz. 359, 71 P.3d 351 (2003) ("Under the
17 due process clause of Arizona's constitution, fundamental fairness is still the
18 touchstone."). Either because it is the right thing to do, or as a sanction, World
19 Phantasy asks the Court to consider and then grant its motion to dismiss claims which
20 do not allege wrongdoing on its part.

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1 RESPECTFULLY SUBMITTED this 12th day of April, 2004.

2 MEYER, HENDRICKS & BIVENS, P.A.

3
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